UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK
Adv. Proc. No. 08-01789-smb (SIPA LIQUIDATION)
- -x
In the Matters of:
SECURITIES INVESTOR PROTECTION CORPORATION,
Plaintiff,
v.
BERNARD L. MADOFF INVESTMENT SECURITIES LLC,
Defendant.
- -x
BERNARD L. MADOFF,
Debtor.
- -x
United States Bankruptcy Court
One Bowling Green
New York, New York

February 25, 2015
10:03 AM

B E F O R E:
HON. STUART M. BERNSTEIN
U.S. BANKRUPTCY JUDGE

08-01789-smb Securities Investor Protection Corporation v.
Bernard L. Madoff Investment Securities

HEARING re Trustee's Motion to Affirm Trustee's Determinations Denying Claims of Claimants Holding Interests in S&P and P&S Associates Partnerships

Transcribed by: Lisa Beck

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P R O C E E D I N G S

THE COURT: Please be seated. Madoff?

(Pause)

MS. VANDERWAL: Good morning, Your Honor.

THE COURT: Good morning.

MS. VANDERWAL: Amy Vanderwal, Baker Hostetler, on behalf of the trustee.

THE COURT: Go ahead.

MS. VANDERWAL: We're here this morning on the trustee's motion to affirm his determination of approximately 158 claims that relate to 36 objections. One objection was received to the trustee's motion.

The claimants invested directly or indirectly with two Florida partnerships, S&P Associates and P&S Associates. Both partnerships had accounts with BLMIS in their names and they were customers at BLMIS. The partnerships filed claims in these proceedings; those claims were allowed. They had received distributions and will continue to receive distributions on the estate.

The trustee's denial over the objecting claimants' claims because they are not customers under SIPA is consistent with several prior decisions of this Court, the district court, the Second Circuit in these proceedings as well as the Second Circuit's decision in Morgan-Kennedy.

Several principles can be distilled from these

decisions that are applicable here today. First, SIPA should be narrowly interpreted on the issue of who is a customer because of the priority treatment granted to customers thereunder. Second, purported customers have the burden of demonstrating that they are deserving of the status thereunder. Third, the critical aspect of the customer definition is the entrusting of their cash or securities to the broker for the purpose of trading securities. And finally and specifically, claimants who did not hold accounts in their name with BLMIS, who did not entrust their funds to BLMIS, who are not known to BLMIS, who did not receive account statements and who are not shown in the books and records of BLMIS are not customers.

Claimants here have failed to carry their burden to demonstrate that they're customers and have provided no evidence that gets around this well settled authority. Indeed, in their responses that were provided to the discovery propounded by the trustee, the claimants have conceded, among other things, that they did not have accounts in their names at BLMIS, they did not directly invest with or make withdrawals from BLMIS and they did not interact with BLMIS. Notwithstanding this, they make two principal arguments in seeking their customer status. The first is that they owned the funds that were invested at BLMIS and second is that they exerted control over investment decisions made by the partnerships. But both of these arguments fail.

First, the assertion that they had any ownership in the funds that were invested with BLMIS is completely untrue. The plain language of both the partnership agreement and Florida partnership law provides that the funds that were invested by the partnerships were owned by the partnerships.

THE COURT: But under prior law, they held the partnership property as tenants in partnership, didn't they? What does that mean?

MS. VANDERWAL: Well, that law was changed as of 1996. And as of 1998, the current partnership law applies to all partnerships (indiscernible).

THE COURT: So you think that if they had a property right in those funds, a change in the law could deny them -- could it be they don't have property rights?

MS. VANDERWAL: First, I would --

THE COURT: Isn't that a violation of due process?

MS. VANDERWAL: I would first argue that even under the prior law, it's questionable whether the level of rights in the property rose to the level of ownership. But even if it did, the due process that was built into the law was that there was a two-year period before the law applied --

THE COURT: Yeah.

MS. VANDERWAL: -- to all partnerships --

THE COURT: But you know --

MS. VANDERWAL: -- that existed over --

THE COURT: -- if you look at the revised act, there's a provision in the revised act which says this law applies to partnerships and any repeal or amendment of this law applies to partnerships. That's provision -- and that's to overcome, I think (indiscernible) or some old Supreme Court case. The Uniform Partnership Act didn't have the same provision.

MS. VANDERWAL: Well, our position that both the partnership agreement and the law that is directly applicable to the partnerships here clearly set out who owns the property. For example, Section 602 -- or 601 -- sorry -- of the partnership agreement clearly provides that the property is owned by the partnership not the partners themselves.

So instead of actually owning the funds that are at BLMIS, the claimants merely made contributions to the partnership. They had an interest in the partnership. They received profits from the partnership. And if they were to withdraw from the partnership, they would receive the value of their partnership interest. They didn't receive any particular property back.

THE COURT: I thought some of the claimants were one or more generations removed also. Were they --

MS. VANDERWAL: Some were indirect. Some were indirect. They directed in the -- they invested in the trust that invested in the partnership. So they were even farther removed from a claim to this property that was invested with

BLMIS.

THE COURT: Do you know how much has been distributed or what the net equity claim is of the two partnerships?

MS. VANDERWAL: I can tell you approximately that one has an alleged claim of approximately two million and the other was approximately 10 million. And so they have received the distributions that all other customers have received to date.

THE COURT: Okay.

MS. VANDERWAL: So, in short, with respect to ownership, the investors in feeder fund in the Second -- the investors here are like the investors in the feeder fund in the Second Circuit decision. They invested in an entity that invested in Madoff. They themselves did not invest in Madoff.

With respect to the second argument that was put forth by the claimants, they cannot demonstrate that they exerted meaningful control over investment decisions. The provision of the partnership agreement that they rely on merely provides that majority consent is required to invest with the broker or withdraw from a broker or grant that broker discretionary investment power. So the control is limited, it's subject to majority rule and it relates only to funds owned by the partnership. Both this Court in the feeder fund decision and the Second Circuit in Kruse have held that demonstrating some level of control over investments or steering those investments to BLMIS is not sufficient to establish customer status where

there are no direct dealings with BLMIS and not that they're not directly invested with BLMIS.

THE COURT: Is there any evidence in the case that you're aware of that the relationship between the partnerships and BLMIS or Madoff is disclosed to the partners prior to Madoff's arrest? I saw the letter after Madoff's arrest.

MS. VANDERWAL: Right. The papers submitted by the claimants suggest that BLMIS was aware that the investors were --

THE COURT: I'm asking if you're aware, for instance, of offering memoranda or anything like that that said you're investing -- the partnership is investing its fund with BLMIS.

MS. VANDERWAL: No. We haven't -- we requested through discovery any information that would suggest that. We haven't received that.

THE COURT: Okay. And Madoff isn't -- or BLMIS isn't mentioned in the partnership agreement, is it?

MS. VANDERWAL: No.

THE COURT: Okay.

MS. VANDERWAL: In sum, we would just submit that the claimants have failed to meet their burden to demonstrate that these funds were entrusted -- these funds that were entrusted to BLMIS were theirs and that they invested them for the purpose of trading securities. So we would request that the

trustee's motion be granted.

THE COURT: Thank you.

MS. GORCHKOVA: Good morning, Your Honor.

THE COURT: Good morning.

MS. GORCHKOVA: Julie Gorchkova of Becker & Poliakoff on behalf of the objecting claimants that were identified on Exhibit A to Ms. Cheema's declaration in opposition to the trustee's motion.

THE COURT: That's that 78 claimants, I believe?

MS. GORCHKOVA: Yes.

THE COURT: Okay. So are the other hundred -- and I'm really asking is are the other half pro se in this? In other words, they filed objections but they didn't respond to the motion?

MS. GORCHKOVA: No. There was only one response received to the motion.

THE COURT: Okay. But there are 158 --

MS. GORCHKOVA: Claims.

THE COURT: -- pro ses --

MS. GORCHKOVA: Some are pro se --

THE COURT: Okay.

MS. GORCHKOVA: Some are represented by other firms. We didn't receive any other --

THE COURT: Okay. Go ahead.

MS. GORCHKOVA: Okay Our arguments are set forth in

our opposition papers so I'm not going to rehash them here. I'd like to instead focus primarily on addressing how the customer opinions in the prior -- how the customer opinions in this case are different from the facts that we have here. And when I state the "customer opinions", what I'm referring to are the earlier decisions involving the trustee's determination of claims that are identified on pages 4 through 8 of the trustee's motion papers and dealt with feeder fund investors and pension plan participants both of which are very different from the relationship that the partners had with BLMIS through the partnerships in this case.

The partners in this case are readily distinguishable from the claimants in the customer opinions in a very material way. When examining the Morgan-Kennedy factors, unlike the claimants in the customer opinions, the partners here have a great deal of control over the actual money that was invested through the partnerships. Indeed, the trustee admits at page 1 of his reply that although he categorizes conditional ability, he nonetheless admits that the partners had an ability to -- had an ability to vote on limited issues relating to how the partnership as a whole would make investments. The partners --

THE COURT: Is there any evidence that that occurred in this case with S&P or P&S? In other words, we know about the 51 percent majority provision. Was there any evidence that the partners acting as a majority, they were selected or fired

a broker or armed the broker with discretionary trading powers?

MS. GORCHKOVA: No. BLMIS -- to my knowledge, BLMIS was the only entity into which the partnerships invested from the --

THE COURT: Well, there was --

MS. GORCHKOVA: -- start of the partnerships.

THE COURT: They signed -- I know they signed the trading agreements about two weeks after the partnership agreements were signed.

MS. GORCHKOVA: I'm sorry?

THE COURT: The trading agreements were signed about two weeks after the partnership agreement was signed.

MS. GORCHKOVA: Correct. And at all times, the partnerships were invested with BLMIS.

THE COURT: But supposedly, at quarterly meetings, the partners were supposed to review the partnerships' relationships with brokers. Is there any evidence in minutes or anything like that that they ever reviewed a relationship with BLMIS?

MS. GORCHKOVA: I have not seen any minutes submitted from our clients. But I know that under the partnership agreement and based on knowledge that I obtained while having discussions with the partners --

THE COURT: That sounds like hearsay.

MS. GORCHKOVA: Right. Nonetheless, I think the

important thing is that it was the ability -- they had the ability to do that irrespective of whether it was done or not.

THE COURT: A majority of the partners had that legal ability, I would agree.

MS. GORCHKOVA: And while the trustee characterizes this as a very limited level of control, we disagree. And we think that in a situation where you have a collective investment, that may perhaps be the greatest level of control that an investor can have --

THE COURT: What do you mean by a collective investment?

MS. GORCHKOVA: Well, for example, under the partnership agreement, only 51 percent of the partnership -- of the interest were required to either change the investments or maintain the investments. For instance, if the partnership agreements require that a 95 percent approval or a 75 percent approval be required, that would be less control than --

THE COURT: What about 60 percent?

MS. GORCHKOVA: Sixty percent would be less control than 51 percent.

THE COURT: What if it said 40 percent?

MS. GORCHKOVA: Forty percent would be greater but it would not be the majority.

THE COURT: But 51 is much more in control, right?

MS. GORCHKOVA: Fifty-one is greater control when you

look -- yes. Fifty-one is the greatest amount of control that you can have when looking at the majority of the partners.

THE COURT: Okay.

MS. GORCHKOVA: Section 804 of the partnership agreement provided for quarterly meetings --

THE COURT: Right.

MS. GORCHKOVA: -- as Your Honor acknowledged. And at the quarterly meetings, the partners were given an opportunity to evaluate whether investment would be maintained with BLMIS or if it would be transferred somewhere else.

THE COURT: Is there any evidence that they even knew that BLMIS was the partnerships' broker?

MS. GORCHKOVA: Yes.

THE COURT: What's the evidence?

MS. GORCHKOVA: Our answers to requests for admissions.

THE COURT: But that's not evidence. Ms. Chaitman signed that. Is she going to testify as to what the general partners told the managing partners or the managing partners told BLMIS? She can't testify to that. That's not evidence.

MS. GORCHKOVA: Ms. Chaitman cannot testify to that. And although you are right that the requests for admissions were signed by Ms. Chaitman only, under the Federal Rules of Civil Procedure, they only need to be signed by -- they can be signed by either Ms. Chaitman or --

THE COURT: I understand that but that avoids the effect of a deemed admission. But the answers are not evidence, are they?

MS. GORCHKOVA: Umm --

THE COURT: How can Ms. Chaitman --

MS. GORCHKOVA: They're not. But --

THE COURT: It would be like her giving an affidavit as to the --

MS. GORCHKOVA: But if it's --

THE COURT: You are not deemed to admit whatever it is the response was. But the response itself is not evidence, is it?

MS. GORCHKOVA: Perhaps not but then the trustee -- if that's -- if Your Honor recognizes that that's a factual issue then the trustee can go forward and take discovery.

THE COURT: How can there be a factual issue without any evidence to raise a factual (indiscernible)?

MS. GORCHKOVA: We think that there is -- that the answers themselves would be sufficient.

THE COURT: Okay. Go ahead.

MS. GORCHKOVA: Furthermore, if it turned out that one of the partners wanted to conduct a vote as to whether the investment would be invested somewhere else or maintained with BLMIS and he was not happy with the result, he also had -- he or she had an opportunity to withdraw from the partnership

within 30 days notice.

THE COURT: That's true about the feeder fund case, though.

MS. GORCHKOVA: Yes. But the feeder fund cases are very distinguishable from the situation that we have here.

THE COURT: But not on the right to withdraw that you just mentioned. Sure, they had a right to withdraw their money from the partnership, right?

MS. GORCHKOVA: Perhaps in that aspect alone. But here, we don't just have the right to withdraw. We have the right to withdraw if they're not satisfied with the vote that happened every three months.

THE COURT: Well, they can withdraw for any reason or no reason, right?

MS. GORCHKOVA: And -- yes.

THE COURT: Okay.

MS. GORCHKOVA: The level of control that the partners had here is very different and more direct than the level of control that was present in the feeder fund decisions. In the first feeder fund decision, the Second Circuit looked at investors who invested into two entities that then invested into hedge funds which then invested with BLMIS. And there, in determining whether the claimants or investors satisfied customer status, one of the things that the Court emphasized was the level of control that the investors had over the feeder

funds' decisions to invest. And there, the Court concluded that based on its review of various feeder fund materials, such as the private placement memoranda, that the investors yielded all of their control to the feeder funds. That is very different from the situation that we have here. And if we look at the private placement memorandum that the Second Circuit actually cited -- that quoted in the decision there, the private placement memorandum stated that the general partner, not the investors, had the sole right to hire and terminate investment advisors. That's precisely the opposite of the situation that we have here in the partnerships agreement.

Now the trustee, in his reply, takes the position that whether the partners retained complete control over the decision regarding the investment as immaterial in light of some of the language in the Second Circuit decision. And he cites -- in his reply papers, he stated "The Second Circuit held in Kruse -- which is the feeder fund decision that I was talking about -- that 'even if appellants could demonstrate that they exercised some level of control over the Feeder Funds' investments, that fact, standing alone, would be insufficient.'"

THE COURT: What else did they say? There's more to that --

MS. GORCHKOVA: He cites --

THE COURT: There's more to that. No.

MS. GORCHKOVA: Yes.

THE COURT: There's more to that quote.

MS. GORCHKOVA: -- "would be insufficient to confer 'customer' status on appellants given that, individually, they 'made no purchases, transacted no business, and had no dealings whatsoever' with BLMIS."

THE COURT: Isn't that what occurred here?

MS. GORCHKOVA: No. First, we would submit that that portion of the Second Circuit decision is not a holding contrary to what the trustee asserted but it's --

THE COURT: But the Second Circuit was quoting more than Kennedy. Wasn't that the holding of Morgan-Kennedy.

MS. GORCHKOVA: No, not to my knowledge.

THE COURT: That's a quote from Morgan-Kennedy that the Second Circuit is quoting in Kruse.

MS. GORCHKOVA: Yes, starting from "'made no purchases, transacted no business, and had no dealings whatsoever' with BLMIS" is a quote from Morgan-Kennedy. But when the Second Circuit made that statement, it was made in the context of -- it actually says the appellants. And the appellants in that case were feeder fund investors which our position is that there are significant -- materially different in a different position than our clients are. And in addition to the fact that we think that that portion is dicta, there's nothing in that decision -- in the Second Circuit decision that

would suggest that that would apply to here, that the same statement would be applied in a different context outside of feeder funds.

Moreover, I don't think it's appropriate to speculate at this point what some level of control the Second Circuit would be referring to.

THE COURT: All right. But can I ask you a slightly different question? Assuming that they had some control but they never exercised it or there's no evidence that they ever exercised it, would that be relevant?

MS. GORCHKOVA: I don't believe so. I think that the Court needs to look at the governing documents just like the Second Circuit looked at the private placement memorandum in the feeder fund case. And if the partners had the authority to exercise a control then that's what the Court should look at as opposed to looking at whether there was an actual exercise of control.

The trustee also cites to the -- relies heavily on the district court's decision in SIPC v. Jacqueline Green Rollover Account which, as Your Honor probably -- is the ERISA account -- is the ERISA decision and this Court's recent decision in connection with the trustee's motion relating to his denial of claims of other plan participants including the Daprex claimants. And he cites those two decisions to argue that the claimants in those cases had a greater deal of control

than the customers -- than the partners have here. And I would submit two things. First, the ERISA decision was limited solely to the issue of how ERISA affects, if at all, the determination of customer status of ERISA plan participants. And although the Court did look at the Morgan-Kennedy factors, it evaluated those factors in the context of -- in numerous contexts in terms of whether a certain argument that was made based on ERISA would somehow impact how one or more factors would be decided. And in fact, in the ERISA decision, the Court specifically said that individual factual issues such as, for instance, some claimants submitted additional evidence showing that they actually had contact with BLMIS or that they made payments directly to BLMIS, the Court declined to consider that. The Court said that those issues that are not related to ERISA specifically is not before the Court and that the bankruptcy court at a later time can determine those individual issues. So the level of control there was not before the Court.

Similarly, with respect to the Daprex decision, I believe that the control that the partners have here is significantly more than the claimants had in the Daprex decision. There, you had participants in pension -- in employee pension plans and, yes, although the participants had the ability to withdraw or invest or rollover their money, they did not have the authority as a whole to control how the money

of the actual plan was invested whereas here, the partners did. Although it was a collective effort, nonetheless that control was there.

And just in terms of some of the other factors that Morgan-Kennedy looks at, as stated in our answers to requests for admissions, the partners that the partnership itself was investing with BLMIS and the partnerships' managing partner, Mr. Sullivan, in fact, told BLMIS that this money was being invested on behalf of partnerships.

THE COURT: So what? So what if they knew that -- I'll grant you that BLMIS knew that these were general partnerships and therefore would know that the investments probably came from the capital contributions of the partners. But what does that mean?

MS. GORCHKOVA: Well, I think it --

THE COURT: Why is that legally significant?

MS. GORCHKOVA: I think it's just another factor that supports a finding of customer status in this particular case. Perhaps not alone, but in Morgan-Kennedy, the Court looked at whether the plan participants were anonymous and not --

THE COURT: Well, weren't they anonymous here? Is there any -- are there any BLMIS records that identify any of these partners?

MS. GORCHKOVA: Not to my knowledge.

THE COURT: So they were anonymous to BLMIS even if

BLMIS knew that they were partners who were investing in the two Florida partnerships that in turn were investing in BLMIS.

MS. GORCHKOVA: Perhaps the identity, the actual identities of the partners, yes. But I think that given that this is a partnership that collectively invested funds, there's also a different level of expectations that the partners have in being deemed customers given --

THE COURT: But can I -- you know, all of these feeder fund -- or most of the feeder fund cases involve limited partnership feeder funds. Isn't the same true with those cases, that BLMIS should have known that they're partnerships and therefore the funds are coming from the contributions of partners?

MS. GORCHKOVA: Perhaps but my point is that in this particular situation where you have partners that retain the control to make the investment decisions that there's a greater expectation for them, that they would be recognized as customers given the fact that they had this control which is distinguishable from the feeder fund cases.

THE COURT: Okay. I got it.

MS. GORCHKOVA: And one other fact that I would just like to address. Although the Florida Partnership Act was amended in 1998 and it no longer provides that the co-ownership of property -- that the partnership properties co-owned by the partners, the reason why we cited it is because I think it's

important because it demonstrates the expectation of the partners when the partnership was formed.

THE COURT: Do you take the position that the new law repealed whatever rights were -- property rights were granted to the partners under the old law? In other words, the trustee is arguing that the old law was repealed and whatever it gave you, you no longer have.

MS. GORCHKOVA: Not necessarily. I think that the partners would be able to opt out of it. I don't know --

THE COURT: Opt out of the new law?

MS. GORCHKOVA: I think they -- because partnership law is generally governed by contract law.

THE COURT: Okay. So you're saying that they could opt out of it through the partnership agreement.

MS. GORCHKOVA: I believe so.

THE COURT: And what does the partnership agreement say in this case?

MS. GORCHKOVA: To my knowledge, it was not amended in light of the change in the law.

THE COURT: But what does the partnership agreement say about the ownership of the property or the individual partner's rights in the property?

MS. GORCHKOVA: The partnership agreement does not talk about the co-ownership of the property, whether --

THE COURT: Sure. Doesn't it say that the partners

can't seek to partake in the property?

MS. GORCHKOVA: Yes.

THE COURT: Okay.

MS. GORCHKOVA: But the partnership agreement also says that upon termination that the partnership assets will be distributed in accordance with the partnership shares. And our position would be --

THE COURT: But every partnership agreement says that. What do you think is going to happen on dissolution or termination? The debts are paid and then the equity is paid out.

MS. GORCHKOVA: One other point that I'd just like to address is the issue raised by the trustee with respect to our answers to the requests for admissions and that they should not be considered by the Court. The trustee cites Rule 33 in response saying that requests for admissions under Rule 33 have to be sworn.

THE COURT: Under Rule 36.

MS. GORCHKOVA: Right. It's Rule 36 -- right. That applies. But under Rule 36, they don't have to be sworn.

THE COURT: I understand. I don't have a problem with how the responses -- with the responses. The fact that they were signed by Ms. Chaitman and that isn't a deemed admission of whatever that particular request was. But that's a different issue from saying that the responder can use the

admissions -- really the denials -- as evidence.

MS. GORCHKOVA: Thank you.

THE COURT: Okay. Anything else? SIPC. I think we should have (indiscernible) for the opposition but go ahead.

MR. KELLEY: Your Honor, Nathanael Kelley for SIPC.

I believe the trustee's counsel has stated the case very clearly and I don't want to repeat what has been said there. And I'll give her the opportunity to respond but I just wanted to offer SIPC --

THE COURT: Your support?

MR. KELLEY: -- support and see if you had any questions.

THE COURT: I have no questions. Thank you.

MR. KELLEY: Thank you, Your Honor.

MS. VANDERWAL: Your Honor, just very briefly. As I mentioned earlier, the six (indiscernible) decisions on four of the trustee's motions as well as Morgan-Kennedy are directly relevant here. In each case, there were separate legal entities in which people invested that, in turn, invested in BLMIS.

In terms of control, as Your Honor recognized, no evidence has been submitted to this Court in terms of exercise of control, in terms of conversations between managing partners and BLMIS. None of that -- there is no evidence of that before the Court at this time. And the other thing --

THE COURT: Suppose there was that evidence in this case, would it then be the trustee's position that they're customers?

MS. VANDERWAL: If they -- just because BLMIS or there were other people who had invested?

THE COURT: Let's say we got an affidavit from somebody who said, you know, I told -- the managing partner told me that this money was going to be invested through the partnership with BLMIS and that's why I did it.

MS. VANDERWAL: And our position is that that would not be sufficient --

THE COURT: Why not?

MS. VANDERWAL: -- because it doesn't satisfy the most essential factor that has been identified from this body of case law which is that the purported customer owned the funds that are invested with BLMIS.

THE COURT: All right. Thank you.

MS. VANDERWAL: Thank you.

THE COURT: S&P Associates and P&S Associates, collectively "the Partnerships", are Florida general partnerships that had accounts with BLMIS and essentially acted as feeder funds investing all of their partnership funds with BLMIS. This motion concerns the customer status of the general partners of the partnerships. They never invested directly with BLMIS. Instead, they invested directly with the

partnerships or indirectly with entities that became general partners of the partnerships and invested their own funds through the partnerships.

For the sake of convenience, I will refer to anyone on invested directly or indirectly with the partnerships as partners.

Except as noted, the facts are not in dispute and are derived from the declarations of Bik, BIK, Cheema, C-H-E-E-M-A, and Vineet, V-I-N-E-E-T, Sehgal, SEHGAL, submitted on this motion and the documents attached to those declarations. The partnerships were formed in 1992 and were governed by nearly identical partnership agreements. Their purpose was to invest in all types of market-placed securities, Partnership Agreements, Section 2.02, and were funded with initial capital contributions by the partners. Partnership Agreements, Section 4.01. Michael D. Sullivan and Greg Powell served as the managing general partners and had the exclusive authority to manage and control the day-to-day operations of the partnership and maintain the partnership property. Partnership Agreements, Section 8.01. Nevertheless, the general partners could have a say in the selection of brokers. For example, a majority of the partners in interest could cause the partnership to terminate or allow a specific broker selected by the majority and grant their selected broker discretionary investment powers with the partnerships' investment funds. Partnership

Agreement, Section 2.02.

In addition, the partnership agreements at Section 8.04 stated that the partners would review any broker's engagement with the partnership at the regular quarterly meetings.

As noted, the partnerships maintained accounts with BLMIS and following the commencement of the SIPA liquidation, filed customer claims with the trustee based on their alleged account statements dated November 30, 2008. According to the trustee, the partnerships' claims have been allowed in an amended amount. Each has received either payment of or the benefit of a 500,000 dollar SIPC advance and interim distributions have been made to each of them from the customer fund maintained by the trustee.

Numerous partners also filed their own customer claims. The trustee disallowed those claims on the basis that the partners were not customers of BLMIS within the meaning of SIPA. One hundred fifty-eight partners objected to his claim determinations and this motion seeks to affirm his disallowance of the partners' claims. The motion elicited the response from 78 partners represented by the law firm, Becker and Poliakoff LLP. Although approximately 50 percent of the objecting partners did not respond to the motion, I will refer to the entire group as the objecting partners.

In SIPC v. BLMIS, 515 B.R. 161 (Bankr. S.D.N.Y. 2014),

the Court reviewed the decisions by this Court, the district court and the Second Circuit relating to the customer status of persons who did not have accounts with BLMIS and instead invested with entities that, in turn, invested directly with BLMIS. To summarize briefly, customer status under SIPA is narrowly interpreted. The "critical aspect" of the customer definition is "the entrustment of cash or securities to the broker-dealer for the purposes of trading securities". The indicia of customer status include a direct financial relationship with BLMIS, a property interest in the funds invested directly with BLMIS, securities accounts with BLMIS, control over the account holders' investments with BLMIS and identification of the alleged customer in BLMIS' books and records. Finally, the claimant has the burden of showing that he or she is a customer, id. at page 165-68.

The objecting partners have failed to sustain their burden of proof. They did not entrust any cash or securities with BLMIS. They invested with the partnerships who, in turn, invested with BLMIS. They have no direct financial relationship with BLMIS. They did not deposit money with or withdraw money from BLMIS or receive investment statements or tax statements in their own names from BLMIS. The documents produced by the trustee show that all communications with or by the partnerships went through Sullivan or Powell and all deposits and withdrawals were made by them in the names of the

partnerships. Thus, even if BLMIS knew or surmised that the partnerships' BLMIS accounts were funded with partners' contributions, there is no evidence that BLMIS maintained records identifying the partners or even knew who they were, and the fact remains that the partners did not entrust anything to BLMIS.

The objecting partners nevertheless contend that the controlling decisions including Kruse v. Bricklayers and Bricklayers and Allied Craftsman Local 2 Annuity Fund, (In re BLMIS), 708 F.3d 422 (2nd Cir. 2013), and SIPC v. Morgan, Kennedy and Co., 533 F.2d 1314 (2nd Cir.), cert. denied. 426 U.S. 936 (1976), are distinguishable for three reasons. First, the partners had a specific interest under Florida law in all partnership property invested with BLMIS. Second, BLMIS knew that each partner had made a decision to entrust his or her funds with BLMIS. Third, the partners had the ability to control the investment decisions because they had the authority to allow or terminate a specific broker and allow a broker to have discretionary investment powers with the partnerships' funds.

The partners had no interest in the property at the partnerships under current Florida law. Florida Revised Uniform Partnership Act ("Florida revised UPA") declares that a partnership is a legal entity distinct from its partners. Florida statute Section 620.8201(1). "Property acquired by a

partnership is property of the partnership and not of the partners individually," id. Section 620.8203, and "Partnership property is owned by the partnership as an entity not by the partners as co-owners", id. Section 620.8501.

In addition, the partnership agreements provide that all property acquired by the partnerships would be owned by and in the name of the partnership and each partner expressly waived his right to require the partition of any partnership property. Partnership Agreement, Section 6.01.

The objecting partners did not dispute the current state of the law or the text of the partnership agreements. Instead, they argue that the partnerships were organized in 1992 under the former Florida Uniform Partnership Act ("Florida UPA") and Section 620.675 of that law provided, among other things, that "at the inception of an incident to the partnership relationship, each partner acquires certain property rights [including] his rights in specific partnership property."

The Florida UPA was repealed by the Florida Revised UPA, effective January 1, 1998, see 6 - Part 1 U.L.A. 24 (2001), but the objecting partners imply that the repeal did not affect the rights granted under the repealed law. Assuming the former law governed the partners' rights, they still had no right to the funds in the partnerships' BLMIS accounts. Former Florida statute Section 620.68 provided that subject to the

Florida UPA and the partnership agreement, a partner could not possess specific partnership property for non-partnership purposes absent the consent of all partners. There is no evidence of such consent here. But even if there was, it would be irrelevant. The partnership agreements provided, as noted, that the partners had no right to the partnership property and waived their right to partition. Accordingly, the partner had no right to possess the partnerships' BLMIS investments under the prior law and certainly has no right in the specific partnership property under the current law.

Next, the objecting partners offered no admissible evidence to support their contention that BLMIS knew that they had invested with the partnerships because they wanted to invest with BLMIS. Instead, the objecting partners cite to their responses to the trustee's request for admissions. The responses were signed by Helen Chaitman, Esquire, the attorney for the objecting partners. And the relevant response consists of multiple hearsay. It is offered to prove that the objecting partners told the managing partners who told BLMIS that the objecting partners were investing in the partnerships in order to invest in BLMIS. It is noteworthy that no objecting partner offered an affidavit to that effect that he told the managing general partners that he was investing in the partnerships in order to invest in BLMIS. Nor did the objecting partners submit an affidavit from either of the managing general

partners attesting to what they told representatives of BLMIS.

Furthermore, the partnership agreements did not mention Madoff, a significant omission given that the partnership agreements were dated December 11, 1992 and that BLMIS trading agreements were dated December 28, 1992. Thus, the partnerships with BLMIS investors from the onset. Nor is there any documentary evidence in the form of offering memoranda or partnership meeting minutes indicating that the partnerships solicited partners with a promise to invest in BLMIS, reviewed and/or approved BLMIS as a broker, invested BLMIS with discretionary trading authority or that the partnership ever informed the partners of its relationship with Madoff or BLMIS until Madoff's arrest. In fact, when Sullivan informed the P&S partners that Madoff had been arrested and all of the partnerships' funds had been invested with BLMIS, his letter did not suggest that the partners already knew that the partnership was invested with BLMIS.

But even if the objecting partners or some of them sought to invest in the partnerships in order to invest indirectly with BLMIS, they still would not be customers. They entrusted their money to the partnerships not BLMIS and they dealt with the partnerships not BLMIS. However, the partnerships hold allowed customer claims and received distributions. The partners have the right under Florida's partnership laws and the partnership agreements to look to the

partnerships to recover at least some of their losses.

Lastly, although the partnership agreements authorized the majority of the partners to direct the partnerships to select or terminate a particular broker or arm a broker with the discretionary trading authority, there is no evidence that this ever occurred. Moreover, the right belonged to 51 percent of the partners acting as a majority and did not empower any individual to dictate an investment, select the broker or withdraw money from BLMIS. As an individual, the partner could only withdraw his investment from the partnership. He had no right or ability to control his "share" of the partnerships' investments with BLMIS.

But even if the partners had some level of control over the partnerships' investments, "that fact, standing alone, would be insufficient to confer 'customer' status on appellants [the partners] given that, individually, they 'made no purchases, transacted no business, and had no dealings whatsoever' with BLMIS." Kruse, 708 F.3d at 427 (quoting Morgan, Kennedy, 533 F.2d at 1318).

Accordingly, the objecting partners have failed to sustain their burden of proving that they are SIPA customers of BLMIS. The Court has considered the objecting partners remaining arguments and concludes that they lack merit. Settle order on notice to counsel to the objecting partners and to the objecting partners that appeared pro se.

Thank you.

MS. VANDERWAL: Thank you, Your Honor.

(Whereupon these proceedings were concluded at 10:47 a.m.)

I N D E X

R U L I N G S

C E R T I F I C A T I O N

I, Lisa Beck, certify that the foregoing transcript is a true and accurate record of the proceedings.

Lisa Beck

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AAERT Certified Electronic Transcriber

Date: February 26, 2015

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